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SUBJECT: IRAQ'S OIL BID ROUND 2: WHAT WILL OPEC SAY?

REF: BAGHDAD 3196

Classified By: Economic Minister Counselor John Desrocher for reasons 1.4 b,d

11. (SBU) Summary: Iraq is currently exempted from Organization of Petroleum Exporting Countries (OPEC) oil production quotas. Iraq's future quota would likely be similar to Iran's current quota of approximately 4.1 million barrels per day. We estimate that Iraq could reach levels of four million barrels per day by 2013. If current plans are successfully implemented (a big "if"), Iraq could potentially further increase production to up to twelve million barrels per day by 2018. This would create significant tensions between Iraq and OPEC members, particularly neighbors (and political rivals) Iran and Saudi Arabia. If Iraq accepts OPEC production limits, it will need to slow its own oil sector growth, negatively impacting investors and economic growth. If the GOI refuses to accept production limits, it could pose a threat to the efficacy and cohesion of the OPEC cartel. Initial reactions at the upcoming December 22 OPEC meeting in Luanda, Angola could provide an early indication whether Iraq's aggressive expansion plans worry the cartel. End summary.

12. (SBU) This cable is one in a series analyzing the impacts of Iraq's Second Petroleum Licensing Round ("bid round"), held December 11-12 in Baghdad. Results of the bid round are detailed extensively in refTel. This cable examines the likely OPEC reaction to Iraq's plans for aggressive expansion of its oil production. Other cables in this series analyze the expected impacts on U.S. firms and why few U.S. oil production companies emerged winners in the second bid round, the impact on Iraq's investment climate and economy, impacts on Iraq's domestic and sectarian politics, and the challenges (notably infrastructure) to attaining Iraq's ambitious production targets.

OPEC Quotas

13. (U) From the June and December bid rounds, the Iraqi Ministry of Oil (MOO) has awarded ten contracts to increase Iraq's oil production by more than 9 million barrels per day. While much can easily go astray (on contracts, timetables, onshore construction, or export infrastructure), Iraq could conceivably be the world's largest exporter of oil within ten years. Iraq is currently exempted from Organization of Petroleum Exporting Countries (OPEC) oil production quotas. Iraq hit peak production of approximately 3.8 million barrels per day (bpd) and averaged 3.5 million bpd in 1979, prior to the Iran-Iraq war, two Gulf wars, and a decade of international sanctions. Iraq has never regained those levels of production, and its current production averages

just 2.4 million barrels per day.

¶4. (C) It is not clear what Iraq's OPEC oil production quota would be once its production and economy recover. OPEC production quotas are based on proven reserves and population. Since Iraq's reserves (115 billion barrels, and likely to rise) are closest to fellow OPEC member Iran's (138 billion barrels), Iraq's quota would likely be similar to Iran's quota of approximately 4.1 million barrels per day. This rough estimate is supported by recent public remarks by Chairman of the Libyan National Oil Corporation Shokri Ghanem, who said OPEC was unlikely to impose renewed quotas on Iraq until Iraqi production reaches "four million barrels per day or so." This estimate also mirrors a comment made privately to Emboffs recently by GOI Deputy Minister of Oil Abdul Karim Laebi.

¶5. (SBU) Based on existing and projected production, we estimate that Iraq could produce four million barrels per day by 2013. If current plans are successfully implemented (a big "if"), Iraq could further increase production to up to twelve million barrels per day by 2018. Former Iraqi Minister of Oil and current Prime Ministerial Advisor Thamer Ghadhbhan told an industry audience on December 7 that "nobody will stop us" from increasing oil production. Ghadhbhan's remark implicitly reiterates the widely-held view in Iraq that other OPEC members have benefitted from Iraq's underproduction for more than twenty years, and it is only fair that Iraq should now get a chance to increase production. One unnamed GOI official aptly summed it up when he told reporters, "OPEC is going to have to give room to Iraq. Iraq has been deprived of its rightful oil sales for decades." Modulating this sentiment somewhat, Minister of Oil Hussain Shahrastani said publicly on December 12 that Iraq would rejoin the OPEC quota system when the time is right, but that "it could be quite some time before we reach the required level of production." However, Shahrastani did not specify what that "required" level of production would be.

Impact on OPEC

¶6. (C) If/when Iraq dramatically increases oil production, it could quickly exceed any OPEC quota by up to several million barrels per day. (Note: OPEC's current total daily production is roughly 28 million barrels per day. End note.) This would create significant tensions between Iraq and OPEC members, particularly neighbors (and political rivals) Iran and Saudi Arabia. If Iraq accepts OPEC production limits, it will need to slow its own oil sector growth, negatively impacting investors and economic growth. If the GOI refuses to accept production limits, it could pose a threat to the efficacy and cohesion of the OPEC cartel. OPEC has several years in which to ponder and then negotiate this issue, but initial reactions at the upcoming December 22 OPEC meeting in Luanda, Angola could provide an early indication whether Iraq's aggressive plans worry the cartel. Post would appreciate OPEC Collective addressees' feedback, as available, on their host government's reaction to Iraq's announced intention to dramatically increase oil production within ten years.

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